

**OPTIONS FOR MUNICIPAL  
TAXES, FEES, AND  
CHARGES: INTERNATIONAL  
COMPARISONS AND THE  
CASE OF POLAND**

Prepared for



East European Regional Housing Sector Assistance Project  
Project 180-0034  
U.S. Agency for International Development, ENI/EEUD/UDH  
Contract No. EPE-0034-C-00-5110-00, RFS No. 608

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October 1996  
UI Project 06610-608

## TABLE OF CONTENTS

PREFACE .....	iii
INTRODUCTION .....	1
Analytical Criteria .....	1
The Polish Context .....	2
LOCAL GOVERNMENTS' FEES AND CHARGES .....	6
User Charges .....	6
Sale or Rental of City Assets .....	11
Fines and Forfeits (post hoc) .....	12
LOCAL GOVERNMENT TAXES .....	12
Property Taxes .....	12
Income Taxes .....	14
Vehicle Taxes .....	14
Sales Tax/VAT .....	15
Use Taxes .....	16
Business Taxes .....	16
Sumptuary Taxes .....	17
Entertainment and Hotel Taxes .....	17
Real Estate Transfer Taxes .....	17
Document Taxes and Stamp Taxes .....	17
SOME OPTIONS FOR POLAND .....	17
Taxes .....	17
Fees .....	18
APPENDIX 1: COUNTRY TABLES .....	19
APPENDIX 2: GRAPHS .....	39
APPENDIX 3: COUNTRY INFORMATION ON PROPERTY TAXES .....	69

## PREFACE

A challenge for effective local government in Poland is to increase the authority of municipalities to generate revenues through taxes, fees and charges. This paper on taxes, fees and charges currently used by municipalities in OECD countries is intended to assist interested parties in considering options. We have been asked to consider the appropriateness and potential for some of these approaches in Poland.

The OECD countries cover a huge range geographically and economically: from established, developed countries like the U.S., Japan, and the European Union countries, to transitional countries like Hungary, the Czech Republic, and Poland itself, which has just become the 28th member of the OECD<sup>1</sup>. The relatively advanced CEE countries tend to be those in the OECD or in the process of becoming members: the Czech Republic, Hungary, and Poland. The available literature about local government fees and charges in OECD countries tends to be statistical, as opposed to analytical. There is more historical experience with, and literature concerning, local government taxes.

This paper is intended to serve as the basis for a workshop which will identify new or under-utilized sources of revenues for Polish gminas, based on international experience. The goal is to identify a limited number of taxes, fees and charges which show substantial revenue potential and could be practically implemented in the near future.

This is a very broad topic, and there are no instant solutions. If consensus on policy issues can be reached, much work would remain to be done on the specifics of particular taxes, fees or charges, and their relation to the system as a whole.

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<sup>1</sup> The OECD countries are: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States.

## **OPTIONS FOR MUNICIPAL TAXES, FEES AND CHARGES: INTERNATIONAL COMPARISONS AND THE CASE OF POLAND**

### **INTRODUCTION**

Throughout the world, local governments get their revenues from their own sources, and by way of grants and subsidies from other levels of government. The tables in Appendix 1 and the graphic materials in Appendix 2 show these major components of local government revenue in selected OECD countries.

Grants and subsidies in OECD countries typically account for 30-40 percent of local governments' revenues. In a few countries (Netherlands and the U.K.), grants are more than 70 percent of local revenues. In a few others (Austria and Sweden), grants are less than 20 percent of local revenues. Grants and subsidies are generally beyond the scope of this paper, although the data in Appendices 1 and 2 include information about grant funding.

Local governments' own source revenues are the focus of this paper. For the most part, own-source revenues consist of (a) fees and charges and (b) taxes. The line dividing these two types of revenue is not absolute, but the former usually involves fees for specific services rendered and charges for specific impacts caused, while the latter includes general revenue raising for general local government purposes. In most countries, taxes account for more local revenues than do fees and charges. In a few countries (Japan and Turkey), taxes account for all local revenues.

In a few OECD countries, capital revenues (derived from sales of capital assets or from non-governmental grants) account for as much as 5 or 6 percent of local revenues. Typically these are countries where privatization of municipal assets is resulting in one-time revenues, such as the Czech Republic, the Netherlands, or Germany.

With regard to these four sources of local revenue—grants, fees and charges, taxes, and capital revenues—Poland's revenue structure appears similar to that of typical OECD countries such as Germany, France, or the U.S., and to transitional economies like the Czech Republic. However, there are important differences that are not captured by the statistics.

While the amount and distribution of revenues used by local governments is important, local control over revenues can also be critical. Local governments' effectiveness and their ability to respond to the needs and desires of their citizens depends to a large extent on their ability to set rates for taxes, fees, and charges. A tax-sharing arrangement, such as exists in Poland with respect to personal and corporate income taxes, under which the national government decides the amount of taxes local governments will receive is in many respects more like a grant mechanism than a local tax. In countries where local governments can set tax rates, they have control over revenues, and are able to respond more effectively to local preferences. Where there is local control over revenues, and where revenues are stable and predictable, long-term borrowing for infrastructure becomes a possibility.

## Analytical Criteria

International experience has shown that four important parameters against which any tax, fee, or charge can be evaluated are:

- **Economic efficiency:** To what extent does the tax, fee, or charge avoid or create undesired distortions in resource allocation? Conversely, does the tax, fee, or charge promote desirable reallocations?
- **Equity:** To what extent are burdens imposed on those who can best afford them, or on those whose behavior generates costs which must otherwise be borne by others?
- **Performance:** How much revenue can be generated, and how stable and buoyant are the revenues generated?
- **Administration:** How complex and how expensive is the administration of the tax, fee, or charge?

## The Polish Context

While understanding options that are being used in other OECD countries is important, it is unlikely that any solution can be copied intact from any other country. In trying to decide what makes sense in the Polish context, it is important to understand:

- **What services Polish municipalities provide:** Services provided at various levels of government vary from country to country, and over time.<sup>2</sup> Different service responsibilities affect both the amount and type of revenue that is needed. World-wide, there is a trend to decentralize service delivery, with local governments assuming more service-delivery responsibilities.
- **What revenue sources are currently used to fund municipally-provided services:** Revenues used to fund operations and maintenance and revenues used to fund replacement or expansion of capital facilities must be understood. Cost recovery practices in both areas should be analyzed. In many countries, including relatively advanced western economies, full cost recovery is not always possible simply because the full costs of providing service have not been analyzed.
- **What revenue authority Polish municipalities currently have and how they use it:** In most OECD countries, there are one or two principal revenue sources for local governments, and a variety of other, but still significant revenues. In most countries, local governments are limited in a variety of ways as to the taxes, fees, and charges

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<sup>2</sup> Locally provided services may not be reflected in local budgets if they are provided by special purpose entities or enterprise. Such entities may be independent or part of the local government. Only the net subsidy to, or profit from, such entities may be reflected in municipal budgets.



they can impose. The nature of these limitations and their effects on tax policy and service pricing must be understood.

This paper is divided into two sections. The first discusses options for local fees and charges, the second options for local taxes. Preceding these two sections, a matrix outlines some of the issues concerning each actual or potential revenue source discussed, and may be a useful discussion tool.

**Table 1**  
**Revenue Source Issues**

Local Revenue Sources	Performance: Revenue Raised or Cost				Possible Improvements	
	Efficiency	Equity	Administrative	Use in Poland?		
<b>Taxes</b>						
Property Tax: based on area	Negative	Poor	Fair	Relatively simple	Yes	Could be converted to a local tax
<b>Property Tax: based on value</b>						
Property Tax: based on value	Neutral	Good	Good	Relatively complex	No	
<b>Income tax surcharge</b>						
Income tax surcharge	Neutral	Good	Good	Relatively simple	No	Rate decisions could be decentralized
<b>Motor vehicle taxes: capt</b>						
Motor vehicle taxes: capt	Positive, d	Good	Good	Relatively simple	Not at local	Could add a local

## Table 1

Performance Metrics and Operational Efficiency									
Local Revenue Sources	Performance Indicators			Operational Efficiency			Financial Health		
	Revenue	Costs	Profit	Efficiency	Quality	Timeliness	Assets	Liabilities	Equity
	Revenue	Costs	Profit	Efficiency	Quality	Timeliness	Assets	Liabilities	Equity
Utility service charges	Positive	Good	Potentially full cost recovery, with targeted subsidies	Good	Good	Potentially full cost recovery, with targeted subsidies	Admission	Yes	Yes
Financial Summary and Outlook									
Utility capital charges	Positive	Good	Potentially full cost recovery	Admission	Limited	Yes			
Residence	Positive	Den	Potential	Admission	At	Yes			





## **LOCAL GOVERNMENTS' FEES AND CHARGES**

Fees and charges for particular services can shift the burden of some expenditures from local governments' general revenues to specific, targeted revenue streams. Revenues collected from those who use, are benefitted by, or create the need for particular services form a separate, identifiable, and pledgeable revenue stream that can be used to pay for the service in question. Although tax revenues remain the dominant source of local government revenues in most OECD countries, there is a world-wide trend toward less reliance on general tax revenues and more reliance on fees and charges.

Because there is perceived equity in a system which requires the user of a service to pay for it, new or increased fees and charges for specific services often meet less popular resistance than new or increased taxes. And, because user charges do not compete directly with central government revenue sources, authority to establish user charges can be more freely granted by central governments than authority to establish local taxes which might compete with central government revenue-raising.

Among the charges that are commonly used in OECD countries are the following:

### **User Charges**

User charges impose some or all of the cost of a particular service on the user or beneficiary of that service. Polish gminas already impose charges for many services, but seldom recover their full costs, especially if capital recovery or replacement is considered. One possible route to increasing revenue, and to putting Polish municipalities on a more sound financial footing, is to increase the extent to which these fees cover the full cost of the service provided.<sup>3</sup>

Among the advantages of user charges as a revenue source are: (1) they tend to increase the efficiency of the service system; (2) they are perceived as more "fair" than general taxes; and (3) they do not compete directly with central government revenue sources. Among the administrative challenges are: (1) determining the optimum rates; and (2) the need to provide exemptions or alternatives for poor people who need services but cannot afford to pay the full charges.

Economists argue that services should be priced at their short-run marginal cost, i.e. the cost of producing one additional unit of the item or service in question. This maximizes the net benefit to the society as a whole: if pricing were higher than the production cost, not everyone who would and could pay the true cost of the service would be able to receive its benefit. When

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<sup>3</sup> Reportedly, the State Anti-Monopoly Board in Poland has determined that municipal service enterprises may not include capital cost recovery in their rates, on the theory that gmina residents have already paid for historical costs in their taxes, and that inclusion in rates would amount to gouging. This contradicts the ideal in most OECD countries of full-cost recovery, towards which mechanisms are created whereby users pay for capital recovery or replacement as they benefit from a service. Specialized rate-regulating bodies may need to be created to address complex pricing issues for communal services, rather than leaving responsibility for this regulation with the same body that regulates commercial and corporate anti-trust issues.

pricing is lower than production cost people (and thus the society as a whole) use services they would not use if they were required to pay the true production cost. When people are allowed to consume services without paying the full cost, the unrecovered cost must be borne by others.

In most OECD countries, pricing is aspirationally the same for all customers, and for all levels of demand, unless there are real differences in service costs (e.g. some water or wastewater service areas may require special lifting or pumping) or unless policy considerations suggest the use of pricing signals to stimulate particular behaviors (e.g. inverse block rates to conserve water while providing all users with a policy-determined reasonable level of service). Pricing may also vary with time, to reflect the higher costs of meeting seasonal or even daily peak demands, and to allow pricing to reduce customers' demand during peak periods.

This general approach can apply to both service charges for operation and maintenance of the system and capital charges for the expansion of the system:

- **Service charges:** These are charges to consumers of a service. They can be made monthly, or on some other periodic basis (e.g. for water and sewer), or they can be imposed at the time the service is actually provided (e.g. bus fares, toll charges). They are often based on the quantity of goods or services consumed. Ideally, rates should be set at a level that reflects the true cost of materials, salaries, supplies, and equipment consumed in the production of the service, plus amortization or depreciation of the cost of capital facilities.
- **Capital charges:** For many services, the municipality's capital cost for the facilities to make the service available can be recovered from the potential user or beneficiary. Examples include development or service availability fees such as those discussed below. Those who will cause the need for expansion of the system can be charged for a proportionate share of the capital cost of the system. For many services, e.g. water and sewer, municipal capacity can only be efficiently expanded in relatively large steps. This implies that there is either excess capacity after such a construction step or capacity shortages before construction, or both. Ideally, the municipality would bring each step of new capacity on-line on a "just-in-time" basis, requiring careful advance planning. In addition to the capital cost itself, the cost of interest and other finance charges can be included in the capital charge.

Examples of user charges and impact fees include:

■ **Utility charges.** In every OECD country, some kind of charges are collected from users of most of communal services, including water, sewer, electricity, telephone, central heating, and hot water. In most countries, the intention is that these charges should fully cover operating costs. There is sometimes a separate calculation and charging mechanism for capital costs, and sometimes a single service charge that covers both capital costs and operating and maintenance costs. Pricing of each kind of municipal service is a complex issue, and economists and regulators can and do spend a great deal of time and energy developing and refining pricing methodologies.



In Poland, user charges do not fully cover costs, even operational costs, for most communal services. Electricity, which is not a local service, is reportedly the exception. Even where authorized to do so, gminas have been reluctant to increase user charges. This may be because of: (1) the potential political cost with respect to voters; or (2) the desire to attract new industries and investment; or (3) there may be structural financial disincentives, such as an off-setting loss of central funds. The reasons for this failure should be clearly understood.<sup>4</sup>

■ **Rent.** The amount of publicly-owned housing in the typical OECD country is far less than in Poland. Where local government housing does exist in other countries, occupants are often charged a subsidized price for the use of housing, so that user charges do not cover the full cost of operation and maintenance, including periodic capital repairs. However, in most OECD countries, only needy applicants meeting a needs-based test are eligible to live in this subsidized housing. An increasingly popular alternative is to increase user charges to cover the full cost, and to provide targeted, needs-based subsidies for those who cannot afford the full cost. Such a program can generate far more revenue than a global subsidy policy.

It is unusual in OECD countries for a local government to own significant amounts of commercial or industrial space. But in the transitional economies of Central and Eastern Europe, where government ownership remains common, it is generally accepted that user charges should, at a minimum, cover the full cost of operations, maintenance, and capital repairs. Market conditions may allow significant profits from such facilities, at least until market forces create significant competition.

■ **Solid waste disposal charges.** These can take the form of collection charges to residents and businesses, and/or tipping fees charged to refuse collection firms. To the extent possible, they should cover the full cost of operation and maintenance, as well as an allowance for the ever-increasing replacement cost of new landfill or other disposal facilities. Because there is a significant and generalized public interest in adequate sanitation, many OECD municipalities subsidize some of these costs from general revenues.

In France, solid waste fees take the form of a "household refuse removal tax." Properties taxable under the property tax on land and buildings are subject to this tax, even if the property or owner is temporarily exempted from paying property taxes. However, industrial properties, and buildings which do not use municipal refuse removal services are exempted by local authorities.<sup>5</sup>

■ **Public transport fares.** As a rule, fares do not cover the full cost of operation of mass transit systems anywhere in the world. Where subsidies are made explicit, they tend to be smaller than when they are concealed in general revenues and expenditures. There are

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<sup>4</sup> USAID-funded work on prices and costs of water, wastewater, solid waste, and district heating is currently being conducted under the DGPA project.

<sup>5</sup> Joan M. Youngman and Jane H. Malme, *An International Survey of Taxes on Land and Buildings* (Boston: Kluwer Law and Taxation Publishers, 1994).

significant external costs that the society avoids when riders use mass transit, so some level of general subsidization is common in OECD countries.

■ **Parking fees.** Parking fees can be imposed on commercial parking facilities and for on-street parking. On-street parking fees can require relatively expensive enforcement and the use of parking meters, parking-vending machines, and/or attendants. However, in urban areas, parking fees can more than pay for all of these administrative costs, and can represent a substantial source of revenue. They also have the salutary effect of reducing urban congestion.

■ **Toll roads/bridges.** The availability of tolls as a source of revenue is extremely site-specific. It depends on the alternatives available to drivers. Where they have no good alternatives, tolls can help assure that drivers pay for the cost of highways and bridges they use. Toll collection can be costly to administer.

■ **Restricted area charges.** Some cities, most notably Singapore, require daily or monthly licenses to drive in congested urban areas, at least at certain times of the day. Such charges approximate the marginal external costs imposed on society when a driver adds one more vehicle to a congested urban area. Where congestion is concentrated in a central area and in specific times, such charges can be used to reduce congestion. Singapore's experience is that these fees have been effective at reducing congestion, but have not raised a great deal of revenue (2 percent of motor vehicle taxes and 1 percent of property taxes).<sup>6</sup>

■ **Education charges.** These include tuition for courses, schools, and kindergartens run by municipalities. Again, there is a generalized societal interest in education and child care, so some subsidization from general revenues is usual in OECD countries. In Poland, responsibility for primary education has recently been transferred to many gminas, and there is an issue about whether adequate revenues have been assigned to cover these expenses.

■ **Health care charges.** Where hospitals or clinics are run by municipalities and where they charge the full cost to those who can afford to pay, and provide needs-based protection for those who cannot, these facilities generate more revenue than when prices are subsidized across the board. However, health care facilities in OECD countries seldom generate enough revenue to cover costs.

■ **Admission charges for parks, recreation, and cultural activities.** As with other services, the starting point is to understand the full extent of costs involved. For some facilities, such as public parks, these costs are relatively low, and the advantages to society of accessible open spaces justify general revenue support. For other facilities, such as concert halls, operas, or theaters, general revenue support may be less defensible, because of the relatively small number of users and their relatively high costs. Needs-based tests are impractical, so a balance must be struck between cost recovery and cultural accessibility.

## Development Fees

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<sup>6</sup>

Watson and Holland (1978) cited in Bahl and Linn, *Urban Public Finance in Developing Countries*.



As a rule, the first three categories discussed in this section apply to new building, or to new commercial or industrial development.

■ **Impact fees.** These are charges to a proposed user of municipal services for the burden, especially the capital infrastructure burden, that the user will place on municipal facilities. Examples include: storm drainage impact fees, parking impact fees, library impact fees, etc. These are usually collected at the time a building or development is permitted or otherwise approved.

In the United States, many local governments have developed fees for impacts development causes on one or more of the following: roads, libraries, storm drainage systems, general municipal government facilities, and school buildings.

In Australia, provisions exist in most states for fees to be charged to a developer to compensate local governments for improvements to roads or other facilities necessitated by the development.<sup>7</sup>

■ **Development taxes.** In France, local authorities can levy a "local infrastructure tax (taxe locale d'équipement)". The tax is assessed on the construction, reconstruction or enlargement of buildings based upon the assessed value of the building. Rural, government buildings and premises in special development zones are exempt from the tax, as are developers who provide infrastructure improvements at their own expense. Other types of property, such as social housing, may be exempted. The local government establishes the rate, which the central government limits to between one and five percent of value. The tax is non-recurrent and is paid in two yearly installments to the central government which administers the assessment and collection of the tax. Although not specifically earmarked, the tax revenue is intended to subsidize infrastructure improvements and services necessitated by the development.<sup>8</sup>

■ **Capital contribution fees, availability of service fees.** These are fees collected from builders, developers, or others desiring service. Basically, the fees are designed to compensate the municipality for the share of a municipality's system capacity (especially water or sewer) that a proposed new building or development will encumber. Such fees are often calculated based on the peak demand of the proposed building or other development.

In the United States, depending on local ordinance, water and sewer availability of service fees can be imposed at the time land is annexed to a municipality and made available for development, at the time a development plan is approved, or at the time a building permit is issued. In Australia, water and sewer availability of service fees can be based on land values.

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<sup>7</sup> Joan M. Youngman and Jane H. Malme, *An International Survey of Taxes on Land and Buildings* (Boston: Kluwer Law and Taxation Publishers, 1994).

<sup>8</sup> id.



■ **Specific construction responsibility.** Although not a fee, a requirement that a builder or developer pay for the cost of distribution lines, water pump stations, sewage lifting facilities, parks, or other municipal facilities required to serve his particular facility acts like a fee by requiring development to pay for itself. If facilities are oversized to anticipate near-term development beyond what a given project actually needs, the developer who first triggers the need can be required to "front-end" the facilities, and reimbursement arrangements can be contractually stipulated that will assure that future developers pay the first developer their fair share.

As a rule, the next category is usually related to infrastructure improvements in existing neighborhoods. Although we have classified them as fees for the purpose of this discussion, they are called fees in some countries and taxes in others.

■ **Betterment levies, special assessments.** These fees assess the cost of public improvements against properties benefitting from the improvements (e.g. a new road, water line, or sewer line). These are sometimes considered taxes, because they can be involuntarily imposed on property owners through no action of their own.

In Sweden local governments may levy street improvement fees based on costs and benefits, as determined by the municipality, in areas where access streets are constructed.<sup>9</sup>

In the U.S., special assessments can be levied against real property benefitted by public improvements such as storm drainage, road improvements, street lighting, and water or wastewater lines. Typically the improvements are financed by a bond issue, over ten to fifteen years, and affected property owners can pay their share (including interest) in annual installments or can prepay the entire amount (and thus avoid interest). The cost is usually shared based on the benefitted properties' frontage or area. The city council's determination of benefit is usually final, in the absence of fraud.

In the Netherlands, a betterment levy may be imposed on real property that benefits from public improvements, including new roads, street illumination, bridges, sewerage systems or parks. The levy may apply for as long as thirty years to allow the municipality to recover a portion (up to 85 percent) of its expenditure for this work. The tax is levied on the owner of the property or the person responsible for municipal property taxes. It is not necessary for the value of the affected property to have risen, although this would be an indication of benefit; but there must be objective evidence that the property has been placed in more advantageous circumstances. The levy is determined by a formula set out in the municipal ordinance. The formula may, for example, relate to the market values calculated for tax purposes, to properties' surface area or volume, or to the length of frontages on the street which has been improved.<sup>10</sup>

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<sup>9</sup> Joan M. Youngman and Jane H. Malme, *An International Survey of Taxes on Land and Buildings* (Boston: Kluwer Law and Taxation Publishers, 1994).

<sup>10</sup> id.

Separately in the Netherlands, a "building sites tax" may be levied when municipal infrastructure prepares a site for development or otherwise improves it. The tax is levied upon the benefitted property, providing that no other agreement exists under which the municipality can recover the cost of the work. The total tax payable may not exceed the cost actually incurred by the municipality. The tax must be adopted within two years of completion of the work. It is normally collected as a single payment, but a taxpayer may choose to pay in up to thirty annual installments.<sup>11</sup>

### **Sale or Rental of City Assets**

Revenues can be generated from sales or rental of municipally-owned real or personal property, from sales of information owned by the city, or from rental of city-controlled space for advertising. Because most OECD countries have relatively little local government-owned property, this is not usually a significant source of revenue.

### **Fines and Forfeits (post hoc)**

Most OECD countries have elaborated systems of fines and forfeits for violations of local ordinances or regulations. With environmental violations, there is often an attempt to tie the amount of the penalty to the harm or potential harm that a violation could cause, and to impose clean-up responsibility on some responsible party in the event of environmental contamination.

Fines for traffic, parking, and other minor infractions have the two-fold purpose of raising revenue and encouraging compliance with local regulations.

## **LOCAL GOVERNMENT TAXES**

In most OECD countries there are one or two key taxes that form the core of local government revenues. For example, in France, special enterprise taxes and property taxes make up two-thirds of local revenues, with a variety of other taxes making up the remainder. In Germany, some 80 percent of local tax revenues come from the income tax, and most of the rest from the property tax. In the U.S., more than 75 percent of local tax revenues come from the property tax, and most of the rest from taxes on goods and services. In all of these countries, there are other, smaller taxes. Details and graphs can be found in Appendix 1.

There are three principal ways by which municipal tax revenues can be increased: (1) by adding new taxes; (2) by increasing the share of taxes allocated by higher levels of government; and (3) by improving tax collection processes. There is limited room in Poland for creation of wholly new taxes because Poland already has, in one form or another, most of the major taxes used by other OECD countries. Some minor taxes could be added, and revenues could probably be increased to some extent, and reliability and stability of fees improved, through better tax

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<sup>11</sup> id.

administration. More importantly, there is probably room for significant improvement in the property tax system and for increased decentralization of the income tax.

A purely local tax would have a locally determined tax base, locally set tax rates and exemptions, local administration, and would accrue to the benefit of local authorities. Such purely local taxes exist in some countries. At the other extreme, some countries control most of these matters at the central level, and allocate some or all of the proceeds to local governments. The more attributes of a tax that are determined locally, the more the tax can be tailored to local citizen preferences and priorities. However, some taxes are difficult to administer effectively at the purely local level.

The following is an outline discussion of the important taxes used in other OECD countries to support local governments.

### Property Taxes

There are many types of property tax, including residential, commercial, and industrial real property taxes, business equipment and inventory taxes, wealth taxes, and estate, inheritance, and gift taxes. Most local governments that rely on property taxes focus on *ad valorem* real property taxes. Appendix 3 lists some of the property taxes currently used in selected OECD countries, and contains a description of the tax, base and rate, exemptions, valuation, and collection procedures.

Taxes on real property are the most important single source of local revenue in many OECD countries. This is especially true in Anglophone countries (Ireland, New Zealand, U.S., U.K., Canada, Australia) and the Netherlands, in all of which it accounts for more than 50% of local taxes. It is somewhat less significant in Italy, France, Japan, and Spain, and still less important in Germany and Austria, though in all of these countries it is a meaningful component of local tax revenues. Property taxes are used only at the central level in Belgium, Greece, and Sweden.

Among the advantages of a real property tax are that: (1) it is a large and robust source of revenue; (2) it is a relatively progressive tax; and (3) it tends not to compete with central government taxes. Among its disadvantages are that: (1) it is politically sensitive at the local level; (2) the value of property owned is not necessarily closely tied to ability to pay; and (3) it can be challenging to administer well.

Design issues for any real property tax system include:

- **What is the tax base?** The site only, or also improvements? Commercial and industrial property only, or also residential? Agricultural? What exemptions? Should this be set nationally, regionally, or locally?
- **What are the tax rates?** Should there be a flat rate or progressive rates? Should different rates apply to different classes of property? Should each jurisdiction be allowed to set its own rate?





- **How are sites and ownership to be identified?** The cadastre system is the core of most OECD property tax systems. There are many approaches to identifying sites and ownership, and they can all be quite expensive if a system must be established from scratch. However, Poland already has an extensive ownership registration system, which could presumably accelerate the process.
- **How should properties be valued and assessed?** Should the value be the annual value, the capital value, or the site value? How are qualified assessors to be identified, trained, and retained? How often are properties to be reassessed? Should there be any automatic adjustments between valuation cycles? Should owners be allowed to self-assess?
- **How should the taxes be collected?** Should there be annual billings? Annual filings by owners? Should taxes only be collected in connection with some event, such as a transfer or exchange? What remedies apply for non-payment?

In Poland, there currently is a property tax based on area, as measured in square meters for residential and commercial property, and on hectares for agricultural property. Such a tax, as opposed to an *ad valorem* tax, tends to encourage economic inefficiencies. There are also equity issues arising from the fact that owners of valuable property pay less, as a percentage of their asset value, than owners of less desirable property. Because such a tax will not capture the rising value of properties, it is also not as buoyant as value-based property taxes.

It appears that while a value-based tax for the benefit of local governments is considered desirable, progress toward such a tax has become bogged down in questions about how to create the national-level structures, including a cadastre system, that are believed to be necessary for a value-based tax system. One possible approach would be to authorize gminas to develop their own property tax systems. The incentives for gminas to create their own system, provided they retain the revenues, are obvious. If this approach is pursued, care should be taken to identify and address any structural disincentives, including subsidy formulas, that would penalize local governments who desire to move forward with a value-based property tax.

## Income Taxes

Individual, and to a lesser extent, corporate, income taxes are significant sources of local tax revenue in many OECD countries. In Germany, they account for some 80 percent of local tax revenues.<sup>12</sup> Japanese local governments levy a progressive income tax on both individuals and corporations which accounts for more than half of local tax revenues. In most Scandinavian countries, there are flat local tax rates that can exceed a 20 percent rate on individual incomes.<sup>13</sup>

<sup>12</sup> *Revenue Statistics 1965-1995*, OECD Paris, ISBN 92-64-04841-3.

<sup>13</sup> Lotz (1981) cited in Bahl and Linn, *supra*, p. 501.

In Sweden these individual income taxes account for essentially all local tax revenues.<sup>14</sup>

Equity considerations can be addressed by a progressive rate structure. Efficiency concerns tend to focus on whether businesses and individuals will locate outside the taxing jurisdiction or avoid activities in the formal sector to avoid the tax, but this is less of a problem where rates are either relatively low or relatively uniform. Income taxes can be stable, buoyant, and productive, but they are difficult to administer at the local level. To avoid the need for extensive and expensive local administration, while still allowing local governments flexibility to set rates, local income taxes can take the form of a “piggy-back” on central government taxes. This solves the administration problem, but is less than full de-centralization because the central authorities continue to control the tax base and enforcement. This intermediate approach could move Poland in the direction of decentralization, and away from a centrally defined revenue-sharing scheme.

The Polish central governments now retains 85 percent of personal income tax revenues and 95 percent of corporate income tax revenues, and distributes the remainder to subnational governments. If Polish policy-makers wanted to move toward more decentralization, they could consider reducing national-level income taxes to rates that would generate the current amount of retained revenue, and leaving it to local authorities to decide whether, and to what extent, to replace or supplement the shared revenues they formerly received.

### Vehicle Taxes

Vehicle taxes can be a reliable, significant, and buoyant source of local revenues. In a country experiencing a rapid increase in automobile usage, such as Poland, vehicle taxes have several advantages: they can be relatively easy to administer, the burden falls most heavily on those with the greatest ability to pay, and they can help recover some of the external costs imposed by vehicle use, including municipal costs for infrastructure construction and maintenance and traffic management. Such taxes tend to increase social and economic efficiency to the extent that they raise the price of operating a vehicle to reflect its true cost. They also tend to decrease congestion and pollution.

Motor vehicle taxes provide a steady revenue stream that can be used to finance municipal road and street improvements, as well as mass transit improvements. Several different kinds of vehicle taxes exist in different OECD countries, and are sometimes used in combination:

■ **Fuel taxes.** An urban fuel tax can raise substantial revenue, is easy to administer, and tends to be progressive. It may also have the incidental effect of reducing urban congestion, although it is not the most effective tax for this purpose. Although there is some concern that people will buy fuel outside of the city limits to avoid city taxes, rural fuel prices are often higher than urban prices (due to transport costs and lack of competition), and this does not seem to be a big problem in practice.

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<sup>14</sup>

*Revenue Statistics*, supra.



■ **Sales/transfer taxes.** A sales or transfer tax on vehicles can generate substantial revenues, and likely be progressive. There is an equity issue, since people who already own cars would not have to pay, while those who newly acquire cars would.

■ **Annual license fees/taxes.** This tax can generate substantial revenues if it is simply structured and properly administered. When the tax is tied to the value of the vehicle, the tax is progressive. Commercial vehicles and buses are often taxed at lower rates. The tax is buoyant, tending to rise with the growth of the local economy. The tax avoids the horizontal inequities of a transfer tax.

Some owners may be tempted to evade the tax by registering their cars in other jurisdictions, but this has not proved to be a widespread problem where taxes do not vary a great deal from one jurisdiction to another. Vigorous enforcement and large penalties can help assure compliance, as can simplified registration and licensing procedures.<sup>15</sup> There are no significant disadvantages associated with this type of tax.

### **Sales Tax/VAT**

Both a general sales tax and a value added tax (VAT) have the potential to generate a significant amount of revenue for local governments. However, in many countries this important source of revenue is reserved for higher levels of government. Such taxes are important sources of local revenue in Austria, Greece, Hungary, Portugal, Spain, Turkey, and the United States (see the graphs in Appendix 2).

Sales tax and VAT are buoyant, and tend to rise with overall economic activity and inflation. Because they use substantially the same tax base, one would ordinarily expect to see either a retail sales tax or a VAT, but not both. While collection costs are significant, a retail sales tax is administratively feasible at the local level, while a VAT generally requires central administration.

Where one city has a higher sales tax rate than other cities, or surrounding jurisdictions, some dislocation may be caused if shoppers and goods are mobile. The larger the informal sector, the greater the potential for evasion.

Sales taxes tend to be regressive, although if retail food purchases (and possibly other basic necessities) are exempted, this regressivity can be essentially eliminated. The most significant income from a sales tax comes from larger purchases, such as appliances, automobiles, and restaurants, so there is not a lot of revenue lost by exempting smaller, necessary purchases.

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<sup>15</sup> Although Indonesia is not an OECD country, it is worth noting that in Jakarta, penalties of 100 percent of tax liability were successfully enforced, if necessary through impoundment of the vehicle. Bahl and Linn, *Urban Public Finance in Developing Countries*, p. 201.

A local sales tax could be locally set and administered, or locally set and centrally or regionally administered. By contrast, local governments' shares of VAT revenue come from revenue-sharing arrangements. These sharing arrangements give local governments less control over revenues than locally-determined taxes, and the sharing formula can often be adjusted by the central or regional government. In this regard, shared VAT revenues operate more like a continuing grant than like a local tax.

### **Use Taxes**

Use taxes are complements to sales taxes, and attempt to address the geographic inequity that would otherwise result from pure "point of sale" sales taxes. Often imposed on automobiles or building materials, use taxes are paid to the jurisdiction where a vehicle is registered, or where a building is constructed, rather than to the jurisdiction where the car dealer or lumber yard happens to be located. Where this approach is used, taxpayers pay either sales tax or use tax, but not both.

### **Business Taxes**

Many different kinds of business taxes are used in OECD countries. The potential revenue can be significant, and they can be politically acceptable, but business taxes are notoriously difficult to administer, particularly in the absence of generally accepted and implemented accounting standards. In theory, such taxes can hinder the development of business in general, or of the targeted businesses or professions. The various forms of business taxes include:

- **Professional taxes:** A tax on the right to practice particular professions, such as lawyers or doctors.
- **Payroll taxes:** Based on the number of people employed by a business, or on their salaries. Among OECD countries, this appears to be a significant source of local revenue only in Austria and Greece.
- **Production taxes:** Based on the number of units produced, or value of production.
- **Construction taxes:** Taxes on the fact or value of construction of private improvements.
- **Utility taxes:** Taxes on the gross receipts of a communal service provider act as a kind of sales tax.

### **Sumptuary Taxes**

Taxes on alcoholic beverages and tobacco can be significant sources of revenue, are consistent with public morality, and are relatively easy to administer. They tend to be regressive, hitting poorer consumers relatively harder than richer.



### Entertainment and Hotel Taxes

Taxes on theaters, movies, cultural and sporting events, as well as on night clubs, casinos, racetracks, restaurants and hotels, can be important in particular cities, especially those with significant tourist attractions. They can be progressive, since more luxurious establishments are often taxed at higher rates. They can be difficult to administer.

### Real Estate Transfer Taxes

Taxes on the transfer of real property, often based on a percentage of the stated value of the property, have obvious negative impacts on efficiency, but can be progressive and politically popular. They do not hit voters directly in large numbers. With an established property registration system, they can be relatively easy to administer.

### Document Taxes and Stamp Taxes

These taxes do not usually generate a significant amount of revenue, though they can cover the costs of providing certified copies, registrations, and other official documents. At higher levels, they can discourage compliance with official regulatory requirements. Care should be taken that the costs of enforcement are not higher than the revenue raised.

## SOME OPTIONS FOR POLAND

On a macro level, it appears that Polish municipalities have a level of revenues that are well within the range of OECD practice. The working group is thus likely to focus on refinements, rather than any new “magic bullet.” The nature of the refinements is likely to be in the general direction of giving municipalities more control over the rate and base of taxation, and more flexibility in establishing fees and charges. Local revenue sources that appear worthy of further investigation at this point include:

### Taxes

- A **value-based property tax** with locally-set tax rates, and possibly local assessment, could contribute significantly to local revenues. If national policy issues preclude a national resolution of this issue, perhaps local authorities could be allowed to pursue local solutions.
- A **locally established income tax** or surcharge, either in addition to, or instead of, the national income tax revenue-sharing formulae could be a significant step in the direction of decentralization.
- Local **motor vehicle taxes**, which are now limited and based on engine size could be increased, based on value, or abandoned in favor of a local fuel tax or fuel tax surcharge.

- Local **hotel, entertainment, and luxury taxes** could provide additional revenue for urban gminas.

## Fees

- **Impact fees** or development levies could help local governments assure that development, especially commercial and industrial development, pays its fair share. Local governments could be granted broad authority to impose such fees, and implementation left to the local level.
- Locally established user charges should have the possibility of recovering up to the full operating and **capital costs** of communal services, public transport, and other services. Although these charges now exist, there is room for improvement. Special consideration could be given to separate analysis of, and possibly separate fees for recovery of, capital and operating costs. A specialized regulatory body, e.g. a public utilities commission, may be necessary if greater freedom to recover capital costs is given to municipalities.
- **Parking fees** could be used to raise revenue and reduce some of the congestion in urban areas. These could be managed by concession or contract. Gminas could be authorized to apply such a system to voivodship and national roads, as well as to their own streets.

In the process of attempting to reach consensus on specific taxes, fees, and charges, it may be helpful to consider some underlying philosophical and policy issues, such as:

- (1) Is decentralization of revenue policy and/or revenue administration to the gminas desired? This question underlies discussions about locally determined taxes, including property and income taxes, fuel taxes, and luxury taxes.
  - If so, how much revenue decentralization is desired?
    - Should gminas have a say in local tax rates?
    - Should they have a say in the tax base for local taxes?
    - Should they define tax exemptions and allowances for local taxes?
    - Can they collect local taxes?
    - Can they assist with collection of national taxes?
  - Is gmina revenue policy a matter of national interest, local interest, or both?
- (2) Can local revenues be identified which do not compete with national taxes?
  - Is cost recovery for municipal services a desirable goal in gmina revenue policy?
    - Where it is not, how should unrecovered costs be addressed?
    - Where it is, how can barriers to full cost recovery be addressed?

## COUNTRY INFORMATION ON PROPERTY TAXES<sup>16</sup>

### DENMARK

#### General Overview

The administration of property taxes is a coordinated effort between the central government and the municipalities. The Central Government's Customs and Tax Administration Agency is responsible for the design of the computer system and the collection and processing of information necessary for establishing the assessment list and establishing property values for taxation. Municipal officials, who work under the guidance of the central government, provide information and administrative support in property assessment and tax collection.

Valuation results, tax billing and collection, land descriptions and sales information have been computerized for several decades. Since 1981, computers have been used extensively in estimating property values. The valuations are used for all taxes based on appraised property values. The computerization of land-related information has permitted extensive coordination among the various land registers.

Taxes levied annually on property include a Land Tax (Grundskyld) on unimproved land and improvements to land, excluding buildings, and a Service Tax (Daekningsafgift) on government and business buildings. These taxes are levied for the benefit of county and municipal governments.

#### Tax Base and Rate

The Land Tax is based on the capital market value of land, and includes improvements to the land, such as drainage, sewerage and roads. The costs of an owner's improvements are assessed and a fixed cost is deducted from the land value for a period of thirty years. The Central Government establishes the tax rate to be levied by the counties, which since 1985 has been one percent of value. Each municipality determines its own land tax rate, but since 1987 the Central Government has prescribed that the rate be between 0.6 percent and 2.4 percent. The average rate of the combined county and municipality levy is 2.3 percent.

The Service Tax is based on the capital market value of buildings and is levied by counties on buildings used by government and its agencies, and by municipalities on commercial and industrial as well as government buildings. The Central Government establishes the maximum tax rates that may be levied by counties and municipalities, and these rates are adopted by nearly all local authorities. The current maximum rate on government buildings for the county levy is 0.5 percent and for the municipal levy, 0.4 percent, totaling 0.9 percent. The maximum municipal rate is one percent of the value of commercial and industrial buildings.

The tax on land of government properties is formally called the Service Tax, since the Land Tax rate is reduced for certain types of government properties.

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<sup>16</sup> Material presented in this appendix is drawn from Joan M. Youngman and Jane H. Malme, *An International Survey of Taxes on Land and Buildings* (Boston: Kluwer Law and Taxation Publishers, 1994).



**Exemptions** The Central Government establishes the categories of property that are exempt from taxation, but, for some categories, permits local discretion in adoption of the exemption. As a practical matter, local governments exempt all properties for which exemptions are allowed. Owners of exempt properties do not make payments in lieu of taxes nor are local governments reimbursed for the loss of taxes. However, government buildings and land are taxable in Denmark, eliminating a major revenue loss experienced by jurisdictions in many other countries. Exemptions are total. Properties which are exempt from taxes include foreign embassies, public areas, transportation and communication properties, public utilities, charitable, educational and religious properties, cemeteries, hospitals defense installations, and historic buildings. Residential buildings are not included in the Service Tax base, but the imputed rental value of owner-occupied residences is subject to income tax. There are no allowances for personal circumstances.

### **Sources of Information**

The computerization and integration of land-related information into a national cadastre has allowed extensive coordination of land registration and property tax administration. The legal register, based upon the German Title Registry system, maintains a continuously updated inventory of all properties which are identified by cadastral parcel numbers. Cadastral parcel numbers are assigned, maps updated, and land area recorded from subdivision plans and measurements provided by private surveyors. All property transfers are registered, and a sales report, which includes the cadastral parcel number, the sale price and mortgage information, must be submitted to the valuation authority. The information is considered to be highly accurate.

Building characteristics and land use regulations are provided by municipal building and planning authorities. Building descriptions, based upon owner questionnaires in 1976, were used to establish a computerized building register. A number of municipalities have conducted field surveys to verify or update information.

The various registers are cross-referenced by cadastral parcel number, property number, address and taxpayer identification number. The system of unique addresses is particularly useful in providing a geographical cross-reference between registers before the geographical coordinates of properties have been recorded. The digitizing of parcel maps and computerization of the legal register are underway and scheduled for completion by years 1995 and 2000, respectively.

### **Valuation**

The various taxes on property are all based on a single appraised value determined according to the property's full cash value at its highest and best economic use. A land value and a total value are estimated for each property. Public regulations, such as zoning or other restrictions on the property's use or alienation, are taken into consideration, but private restrictions are not. Farmland that is expected to be rezoned from rural to urban land will be valued according to its agricultural use until the land is legally transferred to the urban zone, whereupon it will be valued as urban property, even if the agricultural use continues.





The comparable sales approach is used most frequently in establishing appraised values. Where sales are inadequate, the income approach will be used for rental properties and the cost approach for industrial properties.

All properties are to be revalued every four years. In the intervening years, the values are updated annually according to factors reflecting market trends for different property classes in various geographic areas. Individual properties are reappraised annually only when there has been a change to the property that affects its value. The computerized annual indexation and a relatively stable real estate market have made possible extensions of the periods between revaluations in the last decade. Revaluations actually occurred in 1981, 1986 and 1992, which reduced the additional costs related to full revaluation. It is intended that indexing will be replaced with annual revaluations using the capability of the central computerized valuation system. Although the annual indexing has maintained a general assessment level of 95 percent of market value, it cannot maintain the desired degree of uniformity among properties, as measured by the coefficient of dispersion (C.O.D.). C.O.D.'s of 10 to 15 percent at the time of valuation increased somewhat over the years during which indexing was applied, and in a less stable market would be likely to reflect unacceptable inequities.

The valuations are performed by the Central Government, with assistance from local valuation committees in each of 224 valuation regions. There are no specific qualifications or certification requirements for valuers, but many members of the central valuation staff hold advanced degrees in economics or law. Training for Central Government and Municipal Officials is provided by the Training Center for Civil Servants. The estimation of residential values and land values is now fully computerized.

### **Tax Collection**

The property owner is responsible for the payment of taxes which are levied annually. The municipalities determine the number of payments. Typically taxes may be paid in either two or four installments. Only residential owner-occupiers over the age of sixty-five may defer payment. Interest is added to the deferred tax liability. Enforcement of the tax laws is very efficient. Unpaid taxes are registered as a first priority mortgage on the property, and ultimately the property is foreclosed upon by order of the court and sold for payment of the debt. Ninety-nine percent of property taxes are collected.

## **CANADA**

### **General Overview**

Property taxes were levied in Ontario as early as 1784. Over the past twenty years provincial governments have reorganized assessment administration and changed their Assessment Acts to achieve greater equity and uniformity and to ensure a stable source of revenue for local governments and schools. Each of its ten provinces and two territories (here collectively referred to as provinces) provides for the taxation of real (immovable) property and establishes the legal basis and organization for the valuation and assessment of property within

its jurisdiction. There is no federal property tax, and the central government is not directly involved in property tax administration. Property tax revenues primarily benefit local governments, but four provinces collect a jurisdiction-wide property tax.

Provincial governments administer and perform property assessment in six provinces, and in the rest assessing functions are shared between municipal and provincial governments, with the latter generally valuing property in unincorporated areas. In the province of Quebec, municipal governments carry out the primary assessing function under provincial oversight. Assessors, appointed by the province or municipality, establish the assessed value of property within their assessing jurisdictions.

### **Tax Base and Rate**

Unimproved land, improvements to land, and buildings are subject to taxation in every province, based upon their capital value. Tax rates are determined annually in accordance with budget requirements by local governments, and where applicable, by the province or by special taxing districts for schools and other services. In some provinces, tax rates for unincorporated areas are set by the provincial government. The property tax is the primary source of tax revenue available to most local governments.

Nominal rates differ from effective rates in provinces where property is classified and assessed at a percentage of market value. Taxes are imposed on the assessed value of property in accordance with the legal standard prescribed by the laws of each province. In all but two provinces, the same assessment level and definition of value is used throughout each province. In six provinces, this is defined as 100% of market value.

### **Exemptions**

In some provinces, certain exemptions may be adopted by local bylaw. For example, in the province of Manitoba, properties owned by certain charitable and educational institutions are exempted by provincial law from the payment of school taxes on their properties, but exemption from municipal taxes is a matter of local option.

Property owned by an exempt institution but used or rented for non-exempt purposes is generally subject to taxation. The extent to which the property is used for a non-exempt purpose may result in the loss of the exemption entirely or may subject to taxation only that portion used for a non-qualifying purpose.

### **Sources of Information**

Either the province or the primary assessing units in each province collect and manage the information necessary to value property located within their Jurisdictions. Legal descriptions of property and property ownership are recorded in Land Title Registries. The information required to be recorded on deed and title records is governed by provincial law. At a minimum, deeds describe the physical boundaries of the property, and the names of grantors and grantees.



All property transfers and sales prices must be recorded. Parcel identification numbers type of property, mortgage information, and other terms of transfer may be included. Automation of legal registries varies, and some are linked to computers used by property tax officials.

To determine whether sale prices reflect arms-length transactions, assessors solicit information from buyers, sellers or realtors. Some inspect all sold properties, while others inspect sales selectively based on sales ratio analysis.

Assessors collect and maintain information on building characteristics by field inspections. Canada provides strong legal authority to collect information for property assessment. Assessors have legal authority to enter into or on property for the purpose of determining its value. In Quebec, property owners can be fined for refusing entry. Interior and exterior characteristics are collected on all structures.

### **Valuation**

The standard for valuation differs among provinces. It is most often highest and best use, although five provinces prescribe valuation at current use for certain categories of property, primarily for agricultural and forest land. Valuation according to current use is required for all property in four provinces.

All provinces except Quebec provide for the annual assessment of property as of a specific assessment date. Quebec deposits an assessment roll every three years. Changes in property or ownership are revised as they occur for annual tax billing. All but two provinces require by law a periodic reappraisal of all property for assessment purposes. The specific time intervals between reappraisals vary from one to eight years. Individual parcels are revalued if there has been a change to the property due to new construction, demolition, damage, etc. All property must be reinspected during each reappraisal in six provinces. In some provinces, a percentage of taxable parcels must be reinspected on an annual basis. Most provinces use all three approaches to value: comparable sales, replacement cost less depreciation and income. The income approach is most often used for commercial or rental properties.

All but the Province of Newfoundland conduct assessment ratio studies to test the level and uniformity of assessed values. Median and mean ratios are calculated, and in most cases, coefficients of dispersion. Six provinces develop composite province-wide assessment-sales ratios. All of these reported ratios are 80 percent of full market value or higher, with British Columbia, Manitoba, New Brunswick and Quebec at 90 percent or higher.

All provinces report more than 90 percent coverage in actually valuing and taxing real property in their Jurisdictions.

### **Tax Collection**



In all provinces the owners of property are legally responsible for the payment of taxes. Provincial law establishes the legal requirements for notifying taxpayers of their property assessments and taxes. Property taxes are collected on an annual cycle in all provinces with most receiving a single payment.

Tax deferral programs are available to senior citizens in two provinces. In British Columbia, persons over sixty years of age may defer property taxes at current interest rates until their estates are settled. Prince Edward Island limits deferrals to the elderly who qualify for federal income supplements. The interest and deferred taxes constitute a lien on the property until repaid.

The public taking of property for sale at public auction is the usual remedy for tax delinquency. Three years is the most commonly specified period for foreclosure. Penalties and interest are generally applied for late payments, and vary among jurisdictions. All provinces report a high percentage of tax payments are ultimately collected, with collection rates exceeding 95 percent.

## **FRANCE**

### **General Overview**

Tax administration in France is highly centralized under the Direction General des Impôts, an agency of the Ministry of Finance. The Agency assesses the properties, collects the taxes and distributes the proceeds among the various government units.

Property Taxes are imposed on improved (known as built-up) properties, and a Land Tax is levied on unimproved (known as non-built-up) properties on the basis of rental value. In addition, occupiers of residential property pay a Housing Tax. A complete revaluation has not occurred for many years, but periodic updates are accomplished by indexing. Reassessment is a controversial political issue and, as a result, no revaluation plan has as yet been formulated. Solutions to problems related to property assessment and local government taxation are under discussion.

### **Tax Base and Rate**

The tax base is established by the Central Government, and may not be altered by local authorities. Land and buildings are subject to a Property Tax based upon rental value with a deduction of 50 percent for expenses and a Housing Tax based upon rental value of the residence. Land without buildings, not subject to the Property Tax, is assessed and taxed under



the Land Tax on the basis of rental value minus 20 percent for expenses. Property and Housing Tax valuations were established based on rental values in 1970 and have been adjusted periodically by the application of coefficients. In addition, assessed values are multiplied by a general coefficient set by law annually.

Tax rates vary among government units. Since 1981 governments which benefit from the tax revenues have had authority to determine the rate of taxation, but the communal rate must not exceed 2.5 times the average rate for all the communes within a department or the national rate, if higher.

### **Exemptions**

General exemptions apply to government-owned property; property owned by foreign governments, including embassies; property of religious organizations, schools and educational institutions, and cultural institutions, such as museums and historical sites; cemeteries; farm buildings; forest land; and property used for social welfare purposes, such as hospitals, orphanages and civic organizations. Property owned by a tax exempt entity but used for a commercial purpose is taxed as if nonexempt.

New buildings or renovations and changes to existing buildings are exempted from the Property Tax for the first two years after construction. Subsidized low income housing is allowed a fifteen year exemption, and certain other special properties receive exemptions for ten to twenty years. In 1985 approximately seven million buildings or twenty percent of the owners received exemptions.

The Central Government partially compensates local governments for the loss of taxes from exemptions. The grant is awarded in proportion to the reduction in their tax bases, but does not compensate for the temporary property tax exemptions allowed for new construction.

### **Intergovernmental Organization**

Taxes on property are enacted and administered by the Central Government. The only involvement of local officials is in assisting with identification of properties for taxation. Elected members of local authorities gather data on the properties within their jurisdictions. Central Government employees calculate the values, assess the properties, issue tax bills and collect the proceeds. Local governments receive monthly advances based upon the prior year's tax revenues. Taxes are levied simultaneously for all subnational governments and the proceeds are automatically distributed in accordance with the tax rate set by each level. Some local authorities combine into urban communities or districts and have independent fiscal authority which levies taxes in replacement of or in addition to local authorities.

### **Sources of Information**



Ownership and property transfers are recorded in the Fichiers Cadastraux, a register of deeds organized by parcel identification numbers. Owners are required to furnish tax officials with information on physical changes to their property. Tax officials assign the properties to different categories according to their location, characteristics and use. Zoning and environmental conditions are taken into consideration in classifying the properties.

### **Valuation**

The standard for valuation is the rental value of the property as assessed in accordance with annual legally prescribed coefficients enacted into law by the Central Government and periodic adjustments calculated by the central tax administration. In 1991 the general coefficients applied were 1.01 for industrial buildings and 1.03 for other buildings. The index for land values was 1.0. The coefficients are based on general market trends, but the indexes have not kept pace with market rental values. Although the law specifies that property should be revalued every six years and updated every three years, these cycles have not occurred in practice. Changes in properties are taken into account each year and a new value is assessed when the change results in a value greater than ten percent of the prior value.

The valuation process is not yet automated. The values are developed by career service civil servants in the Ministry of Finance who administer various taxes, and are trained to perform their various assignments, which are generally not limited solely to property tax administration. No formal qualifications or certification are required.

### **Tax Collection**

Owners are legally responsible for the payment of Property Taxes and Land Taxes, and occupiers of residential property are responsible for payment of Housing Taxes. The tax bill (avis d'imposition) is sent annually by mail to all taxpayers by the Central Government, and specifies the taxable value, the rates applied by each level of government and the total tax due. There are no procedures for deferral of payment. The taxpayer submits a single annual payment. A current criticism is that the form of notice does not encourage accountability by the various subnational government units since the taxpayer may compare the total tax with prior years, but not scrutinize the individual rates set by the various local authorities.

Tax records and tax bills are fully computerized. The collection ratio is approximately ninety percent. Enforcement of the tax laws is the responsibility of the Central Government, and delinquency in payment of all taxes is governed by the same central laws and procedures. Unpaid taxes become a lien on the property.

## **JAPAN**

### **General Overview**

The present property tax system was established in 1950 as a part of major reform of the entire Japanese tax system. The Ministry of Finance is responsible for administration of national



taxes, and the Home Affairs Ministry has the general administrative responsibility for research, planning and drafting of laws related to local taxation. The Local Tax law provides the legal framework for taxation of property by local governments, which administer and receive the proceeds of four taxes levied on property. The Home Affairs Minister prescribes the methods of assessment and collection for each tax by regulation, known as "The Property Assessment Standard." There are two levels of local government, prefectural and municipal. With the exception of a Real Property Acquisition Tax, all local taxes on property are levied at the municipal level.

Significant increases in land values during the past decade have generated public debate and new initiatives to decrease land speculation and stabilize land prices. The result of these deliberations has been the recent establishment of national policies to increase taxes on land by a variety of means, among them taxes on land-holding, capital gains, and local taxes on property. These tax increases are designed to depress land values, as well as to increase revenue to the national and local governments.

### **Tax Base and Rate**

Local governments levy a Fixed Asset Tax on land, buildings and tangible business assets, a City Planning Tax on land and buildings within urban zones, a Business Office Tax on commercial building space, and a Special Land Holding Tax.

The assessed value for the Fixed Asset Tax and the City Planning Tax is the same, based upon a percentage of current market value, established during the revaluation and fixed for three years. A standard tax rate of 1.4 percent of assessed value, with a ceiling of 2.1 percent, is specified by the Local Tax Law for the Fixed Asset Tax. Land for housing is taxed at 25 percent of assessed value for the portion up to 200 square meters per housing unit and fifty percent of the assessed value for the portion exceeding 200 square meters. Agricultural land in an urban area is also taxed at one-half of its assessed value. The tax rate for the City Planning Tax may not exceed 0.3 percent and is uniformly applied to all properties subject to it.

The Business Office Tax is levied by designated cities both on construction of commercial buildings and on business occupancy of buildings. Business occupancy is taxed at 600 yen per square meter of floor space for buildings over 1000 square meters and 25 percent of the total salaries paid to employees, the company has more than 100 employees.

The Special Land Holding Tax of 1.4 percent of the acquisition cost is imposed annually on the holding of vacant land over a specified minimum size to discourage land speculation. The Fixed Asset Tax is credited against this tax. The tax is also levied on the acquisition of land at three percent of the acquisition cost, reduced by the amount of Real Property Acquisition Tax paid.

### **Exemptions**



Government-owned property and embassies and consulates of foreign countries are exempt from taxes. Property used for educational, religious and social welfare purposes, and as burial grounds, as public roads and by the Red Cross are also exempt.

If the total assessed value of all taxable fixed assets owned in the municipality is less than 300,000 yen for land, 200,000 yen for buildings and 1,500,000 yen for tangible business assets, the owner is exempted from payment of Fixed Asset and City Planning taxes.

The Special Land-holding Tax provides for numerous exemptions, including land used for housing, agriculture and public purposes, or set aside for future municipal use. The Business Office Tax exempts buildings of not more than 1000 square meters from the assets tax and businesses with not more than 100 employees from the tax on salaries.

### **Intergovernmental Organization**

The national legislative body, the Diet, enacts the Local Tax Law which specifies the taxes that can be levied by municipalities, the tax base and tax rate or tax rate range. Although local government may establish a Fixed Asset Tax rate within the range, there are significant disincentives to exceeding the standard rate of 1.4 percent. Municipalities are responsible for administration of local taxes on property, in accordance with the Local Tax Law and standards and methods specified by the National Home Affairs Ministry. Property tax revenues are collected and the proceeds used by local governments. There are no overlapping tax districts.

### **Sources of Information**

Local tax officials collect information on ownership, land and building characteristics and property sales, and maintain parcel maps. Digital maps are not in use. Information on property ownership is acquired from the land registry. Although there is no legal requirement to register property transfers, most owners file with the land registry to protect their property rights. Owners are required to report any alterations made to their property, and tax officials then inspect the property to determine whether the change has affected the property's value.

### **Valuation**

Property is valued at its reasonable market value according to its character and use as of January first in the year of revaluation for Fixed Asset and City Planning Taxes. The valuation methods and procedures are set forth in the Standards for Property Assessment, issued by the Home Affairs Minister.

Land and buildings are valued separately. Land is classified into one of ten categories, and is valued as if vacant. With the exception of rice fields and farms, which include an adjustment for productivity, values are based on comparable sales of similar properties in homogeneous neighborhoods. To foster uniformity throughout Japan, the Minister of Home Affairs establishes a benchmark value for the highest valued land in each prefecture, and the Governor of each prefecture establishes the benchmark value for each municipality. These values are provided by a Central Assessment Council on Fixed Assets, which gathers valuation





information from a number of sources, including local assessors. Local assessing officials then use that value as a point of departure for establishing a street value rating system which determines a standard point value per square meter by neighborhood and block. Adjustments are made to individual parcels based on location, topography and frontage.

Buildings are valued at reproduction cost, based on the current cost of constructing an identical structure or replica with the same materials, design and quality. Separate depreciation factors are applied for wooden and non-wooden structures.

Property is reassessed every three years, and values are fixed for that period. The revaluation is the responsibility of assessors appointed by the Mayor of the municipality. There are no official qualifications for these appointees. The extent of computerization of assessing functions varies among municipalities. The valuation process is generally not automated.

### **Tax Collection**

Taxpayers are notified annually by the local government of the assessed values and taxes due for the Fixed Asset and City Planning Taxes. These taxes are payable quarterly in April, July, December and February.

Taxpayers file returns and pay the amounts due annually for the special land-holding tax. The tax on the holding of land must be paid by May 31. The tax on the acquisition of land is due by the end of February, if the land was acquired during the previous year, or by the end of August, if acquired during the fiscal year ending June 30. The Business Office Tax is also self assessed. Taxpayers must file a return within two months after construction or extension of their property. Returns on business activity must be filed by individuals not later than March 15 and by corporations within two months after the close of the accounting period. The collection ratio is 96.4 percent, including arrears from prior years, and 98.6 percent, if payments in arrears are excluded.

## **THE NETHERLANDS**

### **Tax Base and Rate**

The property tax upon land and buildings was introduced in its current form in 1970. It has two components: one is a tax upon owners and the other is a tax upon users. The municipal council generally sets the tax rate as part of the annual budget process. Since 1990 there has been no limitation upon tax rates, but the owner tax rate may not exceed 125 percent of the user tax rate. Beginning in 1992, taxes are to be administered and collected at the municipal level. Previously, the Tax Office of the Ministry of Finance administered the tax and transferred the proceeds (less costs) to the municipalities.

A municipality may choose between a value base or an area base for the tax. The value base relies upon capital market value and adjusted replacement cost, while the area basis utilizes square meters multiplied by factors for location, use and quality.



Property tax valuations are not currently used for other official purposes, except for valuations by some water defense boards for levying their general property tax. However, this is anticipated to change in the future, with a new valuation statute sent to Parliament in October, 1992. This statute would establish a Valuation Supervision Board to oversee municipal valuations. These valuations would then be used for the central government income tax on imputed rent for owner-occupied property, the net wealth tax and the tax levied by water defense boards.

The property tax rate for combined owner and user taxes is approximately one percent.

### **Exemptions**

Most exemptions relate to the use being made of the property, except in the case of properties administered by public authorities where the exemption relates to the nature of the property. *Primary mandatory exemptions include:* (1) Land professionally cultivated for agriculture or forestry (including buildings on the land, such as greenhouses). Strictly speaking, this is not even an exemption, but a limitation upon the property subject to tax. (2) Improved property used mainly (at least seventy percent) for churches or spiritual societies. If the seventy percent level is not met none of the property is exempt. (3) Estates covered by the Nature Protection Act 1928 (except buildings, which are subject to a special valuation provision) and natural sites administered by nature corporations. (4) Public roads, waterways, lanes for public transportation by rail, and related constructions. (5) Water-defense works and works for the control of water levels, administered by public authorities. (6) Water-purification plants administered by public authorities. (7) Buildings under diplomatic immunity by treaty or decree, including embassies and consulates and international organizations such as the European Community and the International Court of justice.

Municipalities may also grant additional exemptions through their by-laws. Among the exemptions contained in The Netherlands Union of Municipalities *model by-law on property taxes* are rectories and sextons' houses, municipal properties used for public service, public street fixtures, public gardens, parks and cemeteries.

Personal circumstances may affect the collection of the tax, but not the amount of tax levied. If a taxpayer requests a hardship remission, the tax collector will generally try to make arrangements for installment payments. No remission is granted solely to avoid a mortgage upon the property. The extent of remissions has ranged from 0.11 percent to 0.84 percent of total revenues in the period from 1980 to 1989.

### **Intergovernmental Organization**

The property tax is a local tax. Each municipality is responsible for property valuation, either by its own employees or by external contractors. The Mayor and Aldermen are responsible for the assessment of taxes. These tax collections are general municipal revenue, not earmarked for specific purposes. There is no sharing of revenue among different levels of government. The property tax revenue and rates do not affect the distribution of intergovernmental grants. There

is no overlapping of property tax districts, since the tax is limited to properties within municipal boundaries.

### **Sources of Information**

Municipalities have access to an up-to-date version of the National Cadastre with information on property location and boundaries, ownership and legal rights. This information is used in tax valuation and assessment. The taxpayer is obliged to provide any relevant information requested by tax officials. Such requests are most commonly made for the assessment of nonresidential property.

The public notary sends the National Cadastre a copy of each deed issued upon the sale of a property or transfer of property rights. No other official registration of a sale is required. The deed states the address of the property (at least the cadastral parcel number), the names of seller and buyer (lessor and lessee) and the sale price. If only a part of a parcel is sold, the deed will contain a description of the new boundaries.

The cadastral system is fully computerized. Its registers are organized primarily by parcel number, but also indexed by street address and owner's name. Cadastral registration is based upon deed information, and in the event of a conflict between the cadastre and the deed the deed information governs. Cadastral maps-which have a very high accuracy - error less than 1/5 of an inch - are generally used for tax purposes instead of digital maps. The coverage ratio of the tax is 100 percent.

About 55 percent of the municipalities contract with private firms for valuation, but assessment remains a responsibility of the Mayor and Aldermen. Computerized valuation is expanding, with about 25 percent of all municipalities, especially the larger ones, using computerized systems. Officials report costs to be decreasing, due to more efficient valuation systems and strong competition among consultants for municipal contracts.

### **Valuation**

One value is assessed for the entire property, although there may be separate calculations for the land and the buildings. At present municipalities may choose between two systems of property taxation. More than 98 percent utilize a market value base. The alternative tax based upon surface area was at one time used by fifteen percent of the municipalities, but has declined in favor of the value basis.

■ **Value basis.** The value basis utilizes the true economic value of the free and unencumbered right to immediate and complete acquisition of the property in its actual condition. This means the price which the property would fetch if sold in a free market with full vacant possession and without encumbrance or mortgage. This valuation is based on the market value of the property in its highest and best economic use. The valuer may apply any valuation method as long as the result is the value according to the statutory regulations. The comparable sales method is usually used for residential property, while capitalization of rental value is often used for shops.

Unmarketable property is valued at its replacement cost adjusted for depreciation and obsolescence. This only applies to property for which no buyer could be found who would be prepared to pay a price that has a reasonable relation to the free market value and who would be willing to use the property according to applicable land planning rules (zoning). The High Court has held that the adjusted replacement value is the assessed value if the market value is less than 50 percent of the corrected replacement value. Parliament is currently considering a bill that would replace the "reasonable relation" standard by a rule that adjusted replacement value will be taken into account if it is higher than market value.

■ **Area basis.** If a municipality chooses the area basis for the property tax the actual measured area is first adjusted for the property's nature, location, quality and use. Specific multipliers for each of these factors are designed to reflect differences in market values among the properties. Market value is therefore indirectly a factor even in taxation on the basis of surface area.

The measured area is the sum of the surface area of all floors of all structures of built property and the non-built land area in excess of 300 square meters. In principle all the floor space is measured, even if it is not possible to walk erect upon them, but floors that cannot carry a human being are exempted. Generally, the cadastral area will be considered the measured area of property with no buildings, even including a flooded area, such as a river.

The system of multipliers used to arrive at the taxable value of the property is so complex that most municipalities originally using the area basis have changed to the value basis. The cabinet has recommended that the area basis be abolished, and a bill to that effect is under discussion in Parliament.